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UNFAIR FOREIGN TRADE PRACTICES

SELECTED PROBLEMS IN FIVE FAR EAST COUNTRIES

STAFF REPORT

BY THE

SUBCOMMITTEE ON OVERSIGHT AND INVESTIGATIONS

OF THE

COMMITTEE ON ENERGY AND COMMERCE

U.S. HOUSE OF REPRESENTATIVES

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U.S. House of Representatives

Subcommittee on Oversight and Investigations of the Committee on Energy and Commerce

Washington, DC 20515

May 19, 1986

LETTER OF TRANSMITTAL

To Members of the Committee on Energy and Commerce:

It is my pleasure to forward to you a report prepared by the staff of the Subcommittee on Oversight and Investigations entitled, "Unfair Foreign Trade Practices: Selected Problems in Five Far East Countries." This report is the fourth in a series detailing the impact of illegal and unfair foreign trade practices on interstate commerce. This investigation, begun in 1983, has involved eighteen days of public hearings to date and resulted in major changes in U.S. trade and criminal law during the 98th Congress. Further changes in law recommended by the Subcommittee are pending in the 99th Congress.

In February 1986, staff investigators were dispatched to Japan, Hong Kong, Singapore, Thailand, and Taiwan to explore five areas of on-going concern to the Subcommittee. The Subcommittee has long been interested in the efforts to deter fraudulent steel and textile and apparel imports, tariff and non-tariff barriers to U.S. exports, the theft of American intellectual property, and the importations of counterfeit drugs and reimportation of diverted pharmaceuticals.

This report will serve as a basis for further Subcommittee hearings into these topics during the remainder of the 99th Congress.

Sincerely,

John D. Dingell
Chairman
Subcommittee on
Oversight and Investigations

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CONTENTS

Page

INTRODUCTION 1

CHAPTER I - JAPAN 2

Textiles 2
Barriers to U.S. Exports 4

CHAPTER II - THAILAND 7

Textiles 7
Steel 7
Intellectual Property Right Protection 8
Pharmaceuticals 10
Tariff and Non-tariff Barriers 11

CHAPTER III - SINGAPORE 12

Textiles 12
Steel 12
Intellectual Property Right Protection 13
Pharmaceuticals 14
Barriers to U.S. Exports 16

CHAPTER IV - TAIWAN 17

Steel 17
Intellectual Property Right Protection 17
Barriers to U.S. Exports 20

CHAPTER V - HONG KONG 24

Textiles 24
Intellectual Property Right Protection 25
Pharmaceuticals 26

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UNFAIR FOREIGN TRADE PRACTICES

SELECTED PROBLEMS IN FIVE FAR EAST COUNTRIES

INTRODUCTION

During the 98th and 99th Congresses, the Subcommittee on Oversight and Investigations of the Committee on Energy and Commerce published three reports concerning unfair foreign trade practices. These reports were: "Stealing American Intellectual Property: Imitation Is Not Flattery," published in February 1984; "Criminal Components of America's Trade Problem," published in April 1985; and "Barriers to U.S. Exports," published in May 1986.[1]

As a part of the Subcommittee's continuing investigation of unfair and illegal foreign trade practices, several Subcommittee staff members met with a variety of foreign and American businessmen, and government officials in Japan, Singapore, Thailand, Taiwan and Hong Kong earlier this year.

The inquiry focused on five principal areas of concern: steel imports; textile and apparel imports; counterfeit and reimported pharmaceuticals; protection of American intellectual property; and barriers to U.S. exports. The latter two issues led to discussions ranging from the price of California wine in Taiwan to the market for frozen french fries in Thailand.

This report is intended to summarize what the staff delegation learned in each country with respect to each of the subjects investigated.

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[1] Committee Prints 98-V, 99-H, and 99-BB, respectively.

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CHAPTER I - JAPAN

Textiles

The Japanese trade in textile and apparel products is symbolic of the distortions in the international trading system generally occasioned by the emergence of Japan as a dominant player in the world market. The "Japanese model" of promoting exports and minimizing imports to attain national economic prosperity affects all of its trading partners, but particularly the United States.

International trade in textiles and apparel products is governed by the Multifiber Arrangement (MFA), a General Agreement on Tariffs and Trade (GATT)-sanctioned agreement. This is an international umbrella agreement which provides for bilateral agreements between the producers of the developing world and the developed consuming countries. In theory, the MFA was intended to permit the gradual shift of market share in the United States, the European Community and Japan from the higher cost domestic firms to producers in the lower cost developing countries.

In practice, the bulk of textile and apparel imports to the United States has come from countries which have arguably achieved an industrial economy -- Korea, Taiwan and Hong Kong. During the 1980's, the growth in imports was far from gradual. For a number of reasons, some structural and others administrative, the MFA system has simply broken down. The Japanese import only $2 billion worth of textile and apparel products while the United States absorbs $18 billion worth. Fraud has reached epidemic proportions as shippers from our principal trading partners seek to evade the negotiated quotas. The MFA system is no longer fair or efficient.

The discussions with the Japanese focused on both the terms for renewal of the MFA, which is due to expire on July 31, 1986, and enforcement problems that have prevented the United States and Japan from concluding a bilateral agreement. The staff explained the strong Congressional sentiment for three important

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general changes in the MFA: (1) the other developed countries, generally, and Japan, particularly, must agree to a substantially larger share of the imports from the developing world; (2) the U.S. must be able to impose overall limits on textile and apparel imports; and (3) fibers not currently covered by the MFA must be added.

Additionally, the staff conveyed to the Japanese officials the Congressional sentiment that Japan itself can not expect to increase textile and apparel shipments to the United States, and, at least for certain categories, must reduce such shipments. The Japanese were asked to explain their positions on the issues which have produced the delay in concluding a new bilateral agreement.

The Japanese position on the structural issues was multifaceted. In the absence of a bilateral agreement, the Ministry of Trade and Industry (MITI) officials have guaranteed to the United States that MITI will monitor shipments in twenty-four specific categories to assure that previous limits are not exceeded. The Japanese stated that they would do the same with any other specific category the U.S. requested be monitored. However, MITI strongly protested the U.S. position that overall exports, outside specific categories, should also be capped. This position is, they contended, "inconsistent with MFA principles." The staff delegation emphasized that this issue was important to the United States. The staff delegation also raised the issue of Japanese threats to stop exporting certain rayon yarns to the United States. MITI said the matter would be investigated, but noted that if overall shipments are limited, Japan may be forced to change its shipping patterns.

The second critical issue raised by the staff involved the detection and deterrence of fraud. Textile fraud, rampant over the past several years, mostly involves transshipment and false country-of-origin markings to evade quotas on specific products from countries which have reached their limit. One of the larger criminal fraud investigations involves the suspected transshipment of over twenty million square yards of Korean fabric

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through Japan. This fabric is Korean, but is imported into the United States with certificates falsely stating that it originated in Japan. In some cases, this documentation has been prepared by so-called "factoring" merchants in Singapore. Over twenty U.S. importers are the subject of this two-year criminal investigation. Despite requests from U.S. Customs, the Department of Commerce, and the Office of the United States Trade Representative (USTR), the Japanese Government has not been cooperating in the investigation of this multi-million dollar scandal.

The staff delegation discussed the general problem of transshipment and mislabeling of textile and apparel goods in Japan, as well as the specific case of the Korean fabric shipments. The Japanese reaction was cooperative to a point. The staff delegation was told that Japan is working to have a visa system that would provide export registration with the Japanese Government in place by April 1, 1986, and that this should help cut back transshipping. This system has begun operating on a limited basis.

As to the Korean transshipment case, MITI stated that it supported cooperation, but that this was an issue for Japanese Customs and the Ministry of Finance. The staff delegation indicated that the question of cooperation with criminal investigations is basic, should be resolved now, and should not be linked to a new bilateral agreement. The staff asked for MITI's direct intervention with the other agencies. The MITI officials said they would do their best. To date, their "best" efforts have not obtained the assistance of the Japanese firms involved.

Barriers to U.S. Exports

In May 1985, the Subcommittee surveyed over five hundred United States firms and trade associations regarding tariff and non-tariff barriers around the world which significantly inhibited their exports. The responses identified 751 specific foreign trade barriers. As might be expected, Japan headed the list with seventy-two identified barriers, almost ten percent of the total.

The industry complaints which the staff delegation

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discussed in Japan and elsewhere were carefully selected. U.S. firms and government officials have tried for years to convince the Japanese to lower their trade barriers, particularly their non-tariff barriers. The staff discussions in Japan were limited to one general area of concern, technical standards, and one specific area, tobacco.

Technical product standards are major barriers to U.S. exports in developed countries. As in the United States, their primary purpose is to protect consumers from health and safety risks or shoddy workmanship. However, these become trade barriers when, usually with the "assistance" of the domestic industry, they are written to discriminate against imports.

The staff delegation received extensive briefings from the Commerce Department Commercial Attaches at the U.S. Embassy in Tokyo. They made it clear that a major barrier to U.S. exports of manufactured products of all kinds to Japan is the pervasive system of complex technical standards Japan sets for approval of products for sale in Japan. These standards, almost all of which are written exclusively in Japanese, are drafted in close cooperation with domestic industry groups, and often are designed specifically to exclude imports. The famous metal baseball bat case, which took three years to resolve, is a minor example of a major problem. To fight the problem, the U.S. Embassy needs expert personnel and money to have pertinent standards translated and analyzed, and to brief American companies on them. Until this can be done on a systematic basis, American success in breaking into the Japanese market will be limited.

The staff delegation met with representatives of American manufacturers for briefings on negotiations on taxes and tariffs that limit the sale of imported tobacco products in Japan. The staff also met with Japan Tobacco, Inc., the private, government-owned corporation that controls the manufacture and sale of tobacco products, and the Ministry of Finance. Japan needs to reform its system of placing tariffs on tobacco product imports, and then taxing the tariffed cost of the imports. This "tax on tariff" makes imports significantly more expensive than local products. While the market share of imports (two

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percent) has "doubled" since 1981, this is insignificant when compared to potential demand if the import price is reduced and distribution problems are removed. These issues are the basis for a current Section 301 case; however, there is hope that they can be resolved through negotiation.

In discussing the tobacco problem, the Japanese asserted that these issues are not problems, that the tariff was reasonable, that the taxes were uniform, and that distribution was not restricted in any way. Each office tried to pass ultimate responsibility to some other office. It appears that the Japanese do not want to make any serious concessions. It has been suggested that the Japanese may allow imports to increase to about five percent of the market, but no more. If this comes to pass, it will probably not be in the form of actual changes in taxes or distribution, but in some special, ad hoc arrangement to settle the Section 301 case.

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CHAPTER II - THAILAND

Textiles

As was the case in Japan, Thai textile officials were asked for their opinion of the three priority changes which the American producers and many Members of Congress wish included in any new MFA. These were an overall cap on U.S. imports, inclusion of currently exempt fibers, and an increasing share of developing country exports to be absorbed by Japan and the European Community. Their reaction was general -- they understand the desire for a new MFA and are willing to go along, but do not want to see their industry prejudiced. The Thai were cooperative but extremely unhappy about the 1985 embargo and the three-year cutback they suffered because of their textile overshipments. They expressed a strong desire for a more stable trading relationship in the future.

Steel

The Thai are not major steel producers. The domestic industry principally manufactures a small range of pipe and tube products from flat-rolled steel produced abroad, largely in Japan, Korea and Australia. According to the Thai producers themselves, no more than ten to twenty percent of total value is added in this process. Further, they had no real presence in the U.S. market until 1985 after voluntary restraint agreements were signed by the large importing countries.

A serious question arises as to whether Thai pipe should be permitted into the United States at all. The Australians, for example, only permit the importation of Thai pipe processed from Australian sheet steel. The largest Thai pipe producer is ninety-eight percent owned by the Japanese and, thus, the possibility of direct mislabeling of Japanese steel as a product of Thailand is a continuing concern.

The President's program to restrain steel imports for five years to allow the domestic industry to

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modernize will surely fail if substantial new capacity is built in countries such as Thailand, or if such countries are used in fraudulent schemes to enter steel in excess of the negotiated restraint levels.

The staff discussed these matters with both the Thai Government and representatives of the Thai pipe producers. The general impression gleaned from the government trade officials was that, as a poor, developing country, Thailand needed to take advantage of whatever loopholes or "market opening" opportunities might exist in any industry which would yield foreign exchange. They pointed out the special friendship with the United States, as witnessed by our military presence, the joint efforts to disrupt the narcotics trade, and the burden of Cambodian refugees which Thailand has agreed to accept. While each of these circumstances might influence a foreign aid debate, they are less than impressive as excuses for unfair trade practices.

Thai pipe has been assessed a 15.6 percent antidumping duty as a result of an unfair trade case brought by U.S. producers. This has given rise to what might be called a "reverse transshipment" case. The staff delegation learned that one or more Thai producers have been involved in a scheme whereby Thai steel is shipped to Japan, labeled as Japanese product, and sold to the United States. The Thai steel was substandard; yet, the Japanese company charged premium prices for it. Mill test certificates were apparently falsified. Some of the Thai companies had been refusing to cooperate with U.S. Customs agents investigating this fraud. The staff delegation met with these companies and emphasized that their lack of cooperation could result in serious suspicion of Thai involvement in the Japanese fraud. U.S. Customs later informed the staff that the Thai producers had agreed to cooperate.

Intellectual Property Right Protection

Counterfeiting in Thailand is rampant. Fake consumer items, such as apparel, video and audio tapes, watches, and leather goods, are available on street corners throughout Bangkok. The 1978 patent

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law is weak and does not cover pharmaceuticals, agricultural machinery, plant or biological processes or computer data systems. Existing trademark and copyright laws are poorly enforced and penalties are relatively low. Computer software is not specifically covered by copyright law. The staff delegation saw a wide-ranging exhibit of counterfeit and look-alike items at a meeting with the American Chamber of Commerce.

The Recording Industry Association of America estimates that over ninety percent of the market in international repertoire is captured by pirated products. Moreover, a recording industry representative has been denied permission to open an office for enforcement purposes in Bangkok. The staff delegation was told by several Westerners of movie videos that appeared to have been recorded by persons in theaters in the U.S., and then shipped to Thailand for translation and reproduction. Thai lawyers who practice in the intellectual property field confirmed the above-mentioned problems.

Copyright questions are further complicated by the fact that the only countries to which Thailand clearly accords protection are members of the Bern Convention. The United States is not a member. Bilateral agreements in 1921, 1937, and 1968 would seem to provide protection to U.S. authors, but a Royal Decree of 1983, which implemented the existing copyright law, referred only to the Bern Convention. According to a recent Thai court ruling, U.S. authors are not covered under the bilateral agreements, although protection is provided if the work was first published in a country that is a member of the Bern Convention.

The staff delegation met with Thai Government officials responsible for patent and trademark matters. Problems in the coverage of the laws and their enforcement were discussed. Particular emphasis was placed on the potential loss of Generalized Schedule of Preferences (GSP) benefits by Thailand because of inadequate intellectual property protection. The potential gain by Thailand in terms of investment, employment and technology transfer by third countries if intellectual property laws were modernized was stressed as a positive reason for

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action by the Thais.

Pharmaceuticals

Abuse of intellectual property rights is particularly evident in the area of patented medicines. According to the manager of a major American drug manufacturer with operations in Thailand, a generic look-alike of a new U.S. or European drug is available from Thai manufacturers in as little as two weeks after it is introduced to the Thai market. The size, shape, color and some of the markings on the generic copy are identical to the brand name tablet or capsule. The major difference, according to a series of laboratory tests performed by the American company, is that the potency of the copies varies widely. A potency range of between five and two hundred percent was found, along with a distressing tendency to find unidentified foreign material mixed in the compound.

Besides the generics of questionable quality, U.S. firms have suffered a substantial market share loss to counterfeit and stolen goods. Generic sales are reportedly aided by the manufacturers' practice of bribing doctors and pharmacists to prescribe their product. Even worse, however, is the effort by the Government Pharmaceutic Organization (GPO) to convince the Minister of Health to rule that only generic pharmaceuticals -- i.e., Thai generics -- could be used in government health facilities. By a remarkable coincidence, the GPO is also the leading manufacturer of these products. In all, the U.S. manager called the pharmaceutical situation the worst in Southeast Asia.

The virtual loss of the Thai market would not be catastrophic to American manufacturers. But, there could be an impact on American consumers. Thai generics of uneven quality are exported to other countries in the region. Counterfeit "Tagamet," the Smith Kline ulcer drug, has already turned up in Hong Kong. Because of their look-alike nature, it would be a simple matter to repackage them so that they appear to be a product of the U.S. and sell them into the diversion market in this country.

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Tariff and Non-tariff Barriers

Thai import duties are high, especially on U.S. agricultural products. In April 1985, the Thai raised already significant duties on about six hundred items. Wheat, for example, was increased by 108 percent. Tariff increases on apples and cotton were rolled back after the U.S. pointed out that the increases violated Thai GATT obligations. The high tariffs on temperate fruits such as apples, cherries, and peaches are particularly galling because they are not even grown in Thailand. The Government apparently is hoping that farmers in mountains on the Burma border will eventually substitute these fruits for the poppies currently under cultivation.

A leading non-tariff barrier is the Thai Government's failure to approve import licenses for soybeans and soybean oil, which effectively prevents their importation. Potatoes and potato product imports are banned outright.

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CHAPTER III - SINGAPORE

Textiles

The Government of Singapore indicated its strong desire to reach a bilateral textile agreement, and a willingness to cap their overall shipments at reasonable levels, which could include some reductions. They believe the U.S. Trade Representative's current demands for reductions in future textile shipments are excessive. They recognized, even if they did not support totally, the MFA priorities enumerated by the staff.

On the subject of textile transshipments, the Subcommittee staff interviewed the owner of one company who is implicated in "laundering" paperwork for Korean textiles transshipped through Japan. He denied any current involvement, but indicated that until this practice became an issue in United States-Japan negotiations, transshipment and involvement by Singapore trading companies was widespread and extremely profitable. He stated that the practice had dropped off because of the recent publicity, but that it is still taking place.

The Singapore Government officials took the position that unless transshipped goods were physically in the country, they had no basis for investigating or compelling the cooperation of Singapore citizens in the U.S. investigation. In the instant case, for example, while they did manage to persuade the textile trader to come to their offices for an interview, they did not arrange for an interview to be conducted on his premises. Earlier, the Singapore Government had declined a request by U.S. Customs for an opportunity to inspect the textile trader's premises and to review documents associated with certain fraudulent importations.

Steel

The staff delegation met with representatives of Keppel Shipyard, Singapore's largest exporter of steel products. The staff was interested in whether or not

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the value added by Keppel in transforming large steel shapes such as I-beams into prefabricated structural sections for foreign building projects is sufficient to constitute a "substantial transformation" under U.S. Customs regulations. Such a ruling determines whether or not these steel products would be considered to be of Singaporian origin for the purpose of the voluntary steel agreements between the United States and major steel producing countries.

Following a lengthy discussion of steel "transformation", the staff toured the drawing offices and two industrial engineering and fabrication facilities. Although it was obvious that steel shapes are cut, welded, fitted with brackets and have holes drilled into them, it remains to be seen if an independent financial analysis would support Keppel's claim that the value of the steel is increased by forty percent in the process.

Intellectual Property Right Protection

Singapore has been the leading source of audio tape piracy because of its inadequate copyright law. Staff members met with Mr. Herman Hochstadt, Chairman of the Singapore Government Copyright Committee. Mr. Hochstadt and his team provided the staff delegation, along with U.S. Ambassador J. Stapleton Roy, with an informative briefing on the new copyright legislation currently being prepared by the Singapore Government.

Mr. Hochstadt said that the proposed legislation had undergone several revisions after review by international experts, including both governmental and private sector persons from the United States. The bill is expected to be introduced shortly, where it is likely to be referred to a select committee for hearings. Mr. Hochstadt estimated that the new law would be passed before the end of 1986, probably in October or November. While not revealing any specifics of the draft law, Mr. Hochstadt indicated that outside parties would be pleased with the penalty provisions, which have been considerably strengthened over those contained in the initial draft. It was also clearly stated that computer software would be covered by the law, and that it would include

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provisions to join international copyright conventions to conclude bilateral agreements.

Further, Mr. Hochstadt stressed that a bilateral agreement could be concluded shortly after the new copyright provisions are enacted. This would allow U.S. copyright holders to achieve protection before January 1, 1987. This date is important because USTR is charged under the Trade and Tariff Act of 1984 with making a determination on that date as to whether or not developing countries provide sufficient intellectual property protection, in law and practice, to merit the continuation of GSP benefits which, in some cases, represent billions of dollars of duty free exports to the United States market.

It should be noted that in some developing countries, laws are not always effectively enforced. Such a divergence between the law and its effective application has never been a concern in Singapore.

The Subcommittee staff found Mr. Hochstadt to be confident of the legislative timetable and quite willing to address specific concerns raised by U.S. officials and businesses regarding earlier drafts. If passed in the form described, copyright piracy in Singapore should become a thing of the past.

Pharmaceuticals

As a result of extensive review of Food and Drug Administration documents concerning imported pharmaceuticals currently detained, the staff delegation was able to identify several Singapore firms consistently involved as "middlemen" in the transshipment of pharmaceutical products to the United States. One of these "trading" companies involved in several shipments of American Goods Returned is Oscar Pharmaceuticals. The staff delegation met with the manager of this operation, as well as one of the owners. As our concern became evident, the owner pledged his support to assist in the identification of pharmaceutical counterfeiters.

The staff was primarily interested in the shipment of an Eli Lilly antibiotic product, Ceclor, to the United States in the summer and fall of 1985. Although the medicine appeared to be fully potent,

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some of the shipments were found to have been put in counterfeit capsules, with fake lot numbers, labels and packaging. Other shipments were in genuine Lilly packaging. The shipments had come to the U.S. from Singapore and Hong Kong.

According to the chief pharmacist of Oscar, the company bought Ceclor from the J.L. Morrison Company in Malaysia, an authorized Lilly distributor. Oscar's purchase was in response to an order from Galaxy International, a Hong Kong trading company. Oscar said that Morrison was eager to make the sale, even though the volume ordered was too large for Oscar's normal requirements, because sales were low in Malaysia. The Ceclor was delivered to Oscar by Morrison's sales manager, who flew with the goods to Singapore. As instructed by Galaxy, Oscar shipped the goods to Victoria Sales in New York.

J.L. Morrison was not the only company making sales to the Singapore market. In 1985, Multipharmaceuticals offered a range of U.S. products, including Ceclor, Nitrodisk, Durocell and Aldomet, at very low prices. Oscar's chief pharmacist said that the merchandise was suspect -- for example, the Ceclor was in white bottles instead of the usual dark brown -- and Oscar did not buy. The pharmacist said that Multipharmaceuticals had gone out of business. The name and telephone number of Multi's salesperson were provided to Singapore health authorities by the Subcommittee staff. Oscar said that large quantities of Bristol Myer's products were also available on the market in Singapore.

Oscar said that they have not purchased any more Lilly product since the suspect Ceclor. They believe that the largest pharmaceutical broker in Singapore was Satim Pharmaceuticals, a company known to be still active in the resale market. A review of import forms collected by the Food and Drug Administration indicates that Satim was part of at least one chain of resales involving Ceclor.

The staff also met with the Inspection Division of the Ministry of Health. The staff shared its concerns regarding the problems of pharmaceutical transshipment and counterfeits. The Inspection Division performs random sampling and inspection of drugs for sale at

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retail, and also checks the few local manufacturers and repackers. The Ministry of Health also inspects imports, but the percentage of such inspections is very low. The staff was surprised to find that Singapore does not currently require expiration dates on labels.

Generally speaking, if a drug is approved for sale in a developed country, it is legal for sale in Singapore. Legislation implementing a licensing system modeled after that of the United Kingdom is being contemplated. The most recent example of a recall did not involve prescription medication. A Thai-produced facial cream, which was said to be quite popular, was withdrawn from shelves when it was discovered that it contained dangerously high levels of mercury.

Barriers to U.S. Exports

Singapore, like Hong Kong, is basically a free port. Compared to most of the world, barriers to imports are minimal. The Subcommittee had received reports of barriers to the establishment of insurance firms in Singapore. A meeting was held with Mr. Law Song Keng, Director of the Insurance and Actuarial Department of the Monetary Authority of Singapore. The Singapore Government took the position that firms seeking to establish a new business would have to demonstrate a unique service or product not currently available through existing companies serving Singapore. This policy is enforced at the present time in order to preserve the viability of existing underwriters given the limited amount of business currently available.

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CHAPTER IV - TAIWAN

Steel

The staff delegation discussed steel matters with several Taiwanese officials, including two Vice Ministers, and the Vice Chairman of China Steel, the government-owned steel company. The central issue involved the unwillingness of Taiwan to enter into a voluntary restraint agreement similar to those the United States recently negotiated with over fifteen steel producing countries. The Taiwanese reluctance in the face of several unfair trade practice findings regarding certain of their steel imports is puzzling. Apparently, they view the existence of import limiting agreements between the United States and countries such as Japan and Korea as an opportunity to increase their U.S. market share.

For the past decade, the Taiwanese have been adding capacity and upgrading product quality in carbon steel production despite a massive surplus of such capacity in the world. China Steel does sell some of its excess capacity to Japan and claimed that any new capacity not needed for "domestic use" would be channeled to the North. Further, they claimed to be unconcerned that Congress might impose overall limits on steel imports if the President's program continues to produce the disappointing results of 1985 (import penetration rate of 26.5 percent versus a goal of 20.2 percent). Because the President's program is "voluntary," there is nothing to compel Taiwan's participation at this time.

Intellectual Property Right Protection

The staff delegation met with key Republic of China Government officials responsible for laws and regulations pertaining to patents, copyrights and trademarks. Meetings were also held with representatives of the private sector and an excellent briefing was provided by the American Institute in Taiwan. As compared to the situation two years ago, Taiwan has made significant progress in enacting laws

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protecting intellectual property rights. A new copyright law, an amended trademark law, a draft revision of the patent law, and a new draft fair trade law are all praiseworthy achievements. Enforcement, however, has been mixed, and continued strong efforts will be required to realize the full impact of the new laws.

Draft amendments to the patent law were submitted to the Executive Yuan in mid-January 1986. The amendments were still under study at the end of February. After approval by the Executive Yuan, the measure will go to the Legislative Yuan for enactment into law. The National Bureau of Standards, which has responsibility for patents, told the delegation that the new statute will probably be on the books by the end of 1986.

Highlights of the new law include extending product patent protection to chemicals and pharmaceuticals, granting foreign patent holders the right to initiate private complaints, public complaints and civil actions against infringers, reversing the burden of proof in process patent cases for locally-produced products (but not for imports) so that the new producer must demonstrate that the product does not infringe, and increasing the maximum criminal penalty for infringement to five years in jail and a $7500 fine.

The draft law does not cover method of use of chemicals and pharmaceuticals, which is still under study. The Taiwan authorities are also studying a possible bilateral agreement between the American Institute in Taiwan and the Coordination Council for North America based on the Paris Convention. Neither measure appears likely to be implemented soon.

When enacted, the protection for product patents will make the lack of process patents a little less important. However, the National Bureau of Standards said that the law would apply only to new products. Furthermore, existing process patents or even pending applications can not be converted to use or product patents. The lack of coverage of imports is clearly a glaring omission.

One long-standing case involving Monsanto's best-selling herbicide product, Roundup, deserves

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special mention. Despite the fact that Monsanto has valid patents in Taiwan for both the composition of ingredients in Roundup and the process by which the ingredients are assembled, a Taiwanese company, Shin Dar, has been allowed to infringe the patents since 1980. Shin Dar sells the infringing herbicide under the name of glyphosate, which is the active ingredient in Roundup. Shin Dar has a U.S. patent on a process to make glyphosate acid, but the manufacturing process patent carries no right to make and sell compositions of glyphosate and its derivatives. Shin Dar's export sales are made under an exemption from Article 20 of the Pesticides Control Law.

According to the American Institute in Taiwan, Monsanto's 1985 losses in third markets to Shin Dar could be as much as $1.6 billion. Monsanto's repeated efforts to get the Taiwanese authorities to stop Shin Dar's infringement have been unsuccessful. Recently, Monsanto and Shin Dar have reportedly reached an agreement whereby Shin Dar will produce Roundup for Monsanto. This case clearly shows that while Taiwan has made real progress, the patent protection system is quite fragile and has some ways to go before it reaches the standard that obtains in most developed countries.

A new copyright law, explicitly covering computer software, was passed in July 1985. Enforcement regulations, without which the law can not be effectively implemented, were drawn up by the Ministry of Interior and sent to the Executive Yuan for approval in late December 1985. According to the Executive Secretary of the Copyright Committee of the Ministry of Interior, Cabinet approval of the regulations was expected by the end of March. The new law provides for longer jail terms and much higher fines for infringers. A major remaining difficulty for pirated works is the lack of translation rights for U.S. authors. Unauthorized translations of publications such as National Geographic and Child Craft are common.

Discussions were also conducted regarding the treatment of U.S. motion pictures, which were accorded copyright protection in 1985. Technical problems remain relating to the procedures and slowness of the

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mandatory registration process. The registration fee has been reduced to about $30, and notarized copies of ownership certificates are now accepted. However, no picture can be approved without review by the Government Information Office, which has not demonstrated the ability or desire to move rapidly.

A revised trademark law was promulgated in December 1985. Key changes include permitting unregistered foreign firms to bring civil suits in Taiwanese courts, the establishment of a special tribunal or the designation of special judges to handle trademark cases, increases in the penalties and compensation damages, the establishment of a minimum damage provision and the inclusion in liability of unknowing sellers of infringing goods.

A draft law is under active consideration by the Executive Yuan. As written, the bill covers counterfeiting, as well as monopoly, mergers and pyramid schemes. The Vice Minister of Economic Affairs told the staff that the bill would go to the Legislative Yuan this session and could be passed before the end of 1986.

The strongest testament to the improving intellectual property climate in Taiwan comes from representatives of American firms doing business in that country. Two years ago, before Congress conditioned continuation of GSP benefits on respect for intellectual property rights, Taiwan was the undisputed counterfeit capital of the world. Today, American business in virtually all industries affected by intellectual property piracy agree that the Taiwanese legal system does provide meaningful recourse in those areas of the law which have been changed and they fully expect acceptable enforcement of the laws currently under review. This is not to say that Taiwan has eliminated counterfeit products, but the situation has drastically improved, and, in most cases, legal recourse is real.

Barriers to U.S. Exports

The staff delegation met separately with officials of the Customs Administration and the Council of Agriculture to discuss the very high duties that are

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levied on many American industrial and agricultural products. While Taiwanese officials correctly pointed out that they had reduced tariffs on several hundred items since 1979, and some more than once, the staff delegation pointed out that tariffs on many goods were still much higher than would be reasonable given Taiwan's level of development. Furthermore, the staff pressed the Taiwanese officials concerning the ban on the importation of many U.S. products, such as frozen potatoes, peanuts and poultry liver.

Taiwanese officials indicated that the Customs "up lift", in effect, a tax upon a tariff added to imports, had been suspended as of February 1, 1986. Moreover, the draft of new regulations rationalizing the manner by which the value of imported items is determined is before the Executive Yuan for review and final approval. Taiwanese customs officials expected the regulations to be finalized soon. However, the tariffs and conditions on many imports of U.S. industrial and agricultural products remain prohibitive. Despite a $13 billion trade surplus with the United States in 1985 and highly publicized "buying missions" to the U.S. by Taiwanese officials, the overwhelming fact remains that Taiwan continues to protect its domestic industries from meaningful competition.

A case in point is soda ash. The U.S. enjoys a very large international competitive advantage in this basic ingredient for glass production owning to the world's most pure natural deposits. The Taiwanese must produce soda ash through an elaborate and expensive chemical process. In order to protect an industry which is not only relatively inefficient, but also destined to remain that way, they impose a tariff which is excessive, particularly when coupled with a port fee.

Finally, in one of the more ingenious non-tariff barriers encountered, the Taiwanese have decreed that soda ash can only be entered by the ultimate user. Since only one Taiwanese firm is large enough to import an entire boat load of soda ash, the only economic way to ship the commodity, American sales are effectively limited to the consumption of one glass producer. The Government's refusal to permit

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Taiwanese trading companies, agents, or the American exporter to take delivery of a shipment for dispersal to smaller customers is a clear attempt to maintain viability of uneconomic domestic producers.

In another, more highly publicized case, the Taiwanese have long maintained a government monopoly over the production and sale of beer, wine and tobacco products. Last fall, the Administration announced it intended to file a Section 301 complaint to force the Taiwanese to accord "national treatment" to American wine, beer and tobacco products. It was immediately announced that the Taiwanese had agreed to open these markets to American products within six to twelve months. The Administration heralded this as a substantial victory in the war against unfair foreign trade practices.

The Taiwanese agreed to allow "market forces" to determine the sales of American wine, beer and tobacco products within the stated time frame. However, Taiwanese performance to date has not met this promise. Negotiations continue on the implementation of this agreement, including another session scheduled to begin April 29, 1986 in Taipei. However, the August 1, 1986 liberalization date is fast approaching and the Taiwan Tobacco and Wine Monopoly Bureau continues to insist on implementation of conditions that would assure that the American impact on the Taiwanese market will be minimal.

The monopoly insists on maintaining its role as the exclusive distributor of wine, beer and tobacco products. Being a monopoly, it has had no need to advertise extensively and intends to similarly limit the promotional activities of American firms under the "national treatment" rubric. Further, the monopoly is insisting on the right to dictate warehouse fees, sales commissions and even the profit margin permitted American firms. All of these restrictions pale before the real constraint. The Taiwanese are insisting that since the monopoly sets domestic prices at 185 percent of their production costs, that all imported cigarettes, wine and beer must pay a similar tariff in addition to the other costs mentioned above.

All of these factors combine to assure that American products will carry a price three times that

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of their domestic competitors. This will effectively price American wine and beer producers out of all but a very limited luxury good market. American cigarette producers may fare a little better because of the smaller CIF price of their goods, but still will be forced to sell their product at a enormous price disadvantage.

To add insult to injury, last year Taiwan began to market its domestically-produced beer, China Beer, in the United States. While, of course, China Beer pays Federal, state and local taxes which are exactly equivalent to those paid by Budweiser or Miller, it faces no market discrimination. If the Government of Taiwan chooses to raise revenue from the sale of beer, wine and tobacco products, a unit tax could be structured to achieve that purpose without discriminating against U.S. imports. However, to the extent that the Taiwanese insist on maintaining an ad valorem tariff as the revenue raising mechanism and maintaining the other condition of sale restrictions, their agreement to open their market to American wine, beer and tobacco imports must be considered a disingenuous attempt to delay Section 301 retaliation.

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CHAPTER V - HONG KONG

Textiles

Hong Kong is a major importer of textiles into the United States. The British Crown Colony has also been a center of textile fraud. Quotas for U.S. imports are traded on an open market and can be very expensive for certain apparel products in high demand. The quality of Hong Kong goods commands a premium in the United States. All of these factors combine to create enormous incentives for fraudulent activity, primarily transshipment and falsification of country-of-origin designations.

There is no question about the considerable efforts of the Hong Kong authorities to detect and prosecute its citizens who engage in fraudulent activities. Hong Kong also makes a responsible effort to police the quota system and to investigate and prosecute quota fraud.

Hong Kong officials have been particularly concerned with the Textile and Apparel Enforcement Act of 1986 (H.R. 1562), which would significantly impact their imports into the United States. They seem to appreciate the importance of renewal of the MFA and are cognizant that the Congress might override a Presidential veto of H.R. 1562 if a satisfactory extension of the MFA is not achieved by July 31, 1986.

The Hong Kong officials indicated their support for an increased share of imports by Japan and other developed countries. They objected to aggregate limits and seemed to accept grudgingly that shipments of ramie and other non-MFA fibers might be covered by a new agreement.

As might be expected, they protested vigorously the new U.S. Customs restrictions on entries valued below $250 and were encouraged to hear that the U.S. Customs Service was willing to accomodate legitimate sample shipments.

Hong Kong is a free port, and the question was raised as to why the volume of U.S. exports to Hong Kong has been so low. Hong Kong officials told the staff delegation that if the U.S. textile industry was

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willing to be more flexible on price and delivery terms, they believe there is a significant market for U.S. textile piece goods in both Hong Kong and Singapore since Japanese goods are becoming more expensive as the Yen rises in value.

The staff delegation had an opportunity to tour several apparel factories in Macao. Macao is technically a Portugese colony; however, its ties to mainland China are substantial, and its economy is interwoven with that of Hong Kong.

Macao had recently adopted the Chinese requirement of a six-day work week. However, two of the three factories visited on a Sunday appeared to be operating at full capacity. When the managers were questioned about the labor laws, they indicated that any labor law could be ignored with impunity.

Working conditions appeared to be cleaner than might be expected, perhaps in anticipation of the visit by the staff delegation, but ventilation appeared minimal and the factories would likely be very unpleasant in the warmer months. The staff delegation was told that, on average, these workers earn about $50 U.S. dollars per week for forty-eight hours of work in Macao, about one-half of the average Hong Kong wage for apparel workers.

Intellectual Property Right Protection

The scope of laws protecting patents, trademarks and copyrights in Hong Kong is excellent and enforcement is vigorous. The staff delegation reviewed the situation with officials of the Trade and Customs Departments of the Hong Kong Government, as well as several representatives of concerned private sector companies. The staff also met with the Industrial Property Investigation Division of Customs, the office primarily responsible for investigating trademark and copyright violations. The staff reviewed the impressive collection of seized goods, including fake Apple and IBM computers, video games, apparel and medicinal products.

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Pharmaceuticals

The staff delegation met with a Chinese employee of Elmcrest Trading, one of the firms that transshipped Ceclor to the United States. Elmcrest bought the Ceclor through a clinic in Hong Kong, Chung Ching. The goods were sold to Sona Distributors, a Miami, Florida importer. The Elmcrest employee explained that the firm usually bought through clinics, and always sold to Sona. The clinics normally bought from manufacturers representatives at favorable prices. Sometimes, Sona would request the specific pharmaceuticals in advance. Other times, Sona would leave the selection to Elmcrest. The Ceclor was bought from the Eli Lilly agent in Hong Kong. The employee added that in mid-1985, Chung Ching showed him some Ceclor from Singapore, but Elmcrest did not buy it because the color of the bottles was unusual.

The owner of Elmcrest, Mr. Indra Chawla, was in the United States on business during the interview. The Elmcrest employee said that Mr. Chawla could be contacted through Sona. He also said that Elmcrest did business with pharmaceutical wholesalers in Singapore that were owned by ethnic Indians. He recalled the name Satim, adding that he had heard his boss, Mr. Chawla, speaking in Indian while arranging drug deals over the telephone with companies in Singapore.

The Elmcrest employee recalled shipping a Johnson and Johnson topical ointment, and Serex, a Wyeth product, to Sona. The staff was shown manufacturers' invoices for Pavabid capsules and Bretyol ampules from Marion Laboratories.

The staff, accompanied by U.S. Customs personnel, next went to visit Galaxy International, another company that had shipped Ceclor to the U.S., according to entry documents collected by the Food and Drug Administration. The group accidentally walked in on another company with a similar name, Galaxy International Production Company. This Galaxy was a modeling agency and a China trading company. The wife of the owner explained that the firm was not in the pharmaceutical business -- at least not yet. When

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asked to explain, she said that the company had plans to purchase expired pharmaceuticals from a doctor in Bakersfield, Califoria and sell them to China. She further assured the staff that if the sale of expired pharmaceuticals to China posed any problems for U.S. authorities, they could easily arrange to have them repackaged.

The staff then found the genuine Galaxy International, whose owner, Mr. K. Jeswani, did not appear to be at all surprised by a visit from U.S. Congressional staff. In fact, he had been called by Oscar Pharmaceuticals in Singapore, of which he is part owner. He said he bought the Ceclor from Oscar and had it shipped directly to the U.S. Mr. Jeswani said he sold the Ceclor to a Parisian firm called Natalie, Inc., headed by Mr. Neev Vigdor. Whatever the truth of this statement, Mr. Vigdor owns and operates a firm in Miami, Florida under the same name. Natalie told Galaxy they were interested in buying Ceclor, so Mr. Jeswani bought the goods from Oscar. Mr. Jeswani said he was now out of the pharmaceutical business and would concentrate on his primary business, buying and selling health and beauty aids, especially perfumes.

While the staff interviewed Mr. Jeswani, Galaxy employees in the next room were busily at work changing and removing country-of-origin labels on boxes of health and beauty aids apparently destined for the United States. Mr. Jeswani said he sold to Interstate Cigar Corporation and Quality King, both U.S. firms.

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